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H. R. 1949

To amend the Internal Revenue Code of 1986 to provide a capital gain exclusion for investments in qualified businesses with employee stock ownership programs within Federal enterprise zones.

IN THE HOUSE OF REPRESENTATIVES

APRIL 29, 1993

Mr. WELDON (for himself and Mr. ANDREWS of New Jersey) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to provide a capital gain exclusion for investments in qualified businesses with employee stock ownership programs within Federal enterprise zones.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That (a) chapter 1 of the Internal Revenue Code of 1986
4 (relating to normal taxes and surtaxes) is amended by in-
5 serting after subchapter T the following new subchapter:

6 **Subchapter U—Capital Gain Exclusion For**
7 **Investments In Enterprise Zones**

“Sec. 1391. 100 percent exclusion for gain from new zone investments.

“Sec. 1392. Enterprise zone business defined.

“Sec. 1393. Tax enterprise zone.

1 **“SEC. 1391. 100 PERCENT EXCLUSION FOR GAIN FROM NEW**
2 **ZONE INVESTMENTS.**

3 “(a) GENERAL RULE.—Gross income shall not in-
4 clude 100 percent of any qualified capital gain recognized
5 on the sale or exchange of a qualified zone asset held for
6 more than 5 years.

7 “(b) QUALIFIED ZONE ASSET.—For purposes of this
8 section—

9 “(1) IN GENERAL.—The term ‘qualified zone
10 asset’ means—

11 “(A) any qualified zone stock,

12 “(B) any qualified zone business property,

13 and

14 “(C) any qualified zone partnership
15 interest.

16 “(2) QUALIFIED ZONE STOCK.—

17 “(A) IN GENERAL.—Except as provided in
18 subparagraph (B), the term ‘qualified zone
19 stock’ means any stock in a domestic corpora-
20 tion if—

21 “(i) such stock is acquired by the tax-
22 payer on original issue from the corpora-
23 tion solely in exchange for cash,

1 “(ii) as of the time such stock was is-
2 sued, such corporation was an enterprise
3 zone business (or, in the case of a new cor-
4 poration, such corporation was being orga-
5 nized for purposes of being an enterprise
6 zone business), and

7 “(iii) during substantially all of the
8 taxpayer’s holding period for such stock,
9 such corporation qualified as an enterprise
10 zone business.

11 “(B) REDEMPTIONS.—The term ‘qualified
12 zone stock’ shall not include any stock acquired
13 from a corporation which made a substantial
14 stock redemption or distribution (without a
15 bona fide business purpose therefor) in an at-
16 tempt to avoid the purposes of this section.

17 “(3) QUALIFIED ZONE BUSINESS PROPERTY.—

18 “(A) IN GENERAL.—The term ‘qualified
19 zone business property’ means tangible property
20 if—

21 “(i) such property was acquired by
22 the taxpayer by purchase (as defined in
23 section 179(d)(2)) after the date on which
24 the designation of the tax enterprise zone
25 took effect,

1 “(ii) the original use of such property
2 in a tax enterprise zone commences with
3 the taxpayer, and

4 “(iii) during substantially all of the
5 taxpayer’s holding period for such prop-
6 erty, substantially all of the use of such
7 property was in a tax enterprise zone and
8 in an enterprise zone business of the tax-
9 payer.

10 “(B) SPECIAL RULE FOR SUBSTANTIAL IM-
11 PROVEMENTS.—The requirements of clauses (i)
12 and (ii) of subparagraph (A) shall be treated as
13 satisfied with respect to—

14 “(i) property which is substantially
15 improved by the taxpayer, and

16 “(ii) any land on which such property
17 is located.

18 For purposes of the preceding sentence, prop-
19 erty shall be treated as substantially improved
20 by the taxpayer if, during any 24-month period
21 beginning after the date on which the designa-
22 tion of the tax enterprise zone took effect, addi-
23 tions to basis with respect to such property in
24 the hands of the taxpayer exceed the greater of
25 (i) an amount equal to the adjusted basis at the

1 beginning of such 24-month period in the hands
2 of the taxpayer, or (ii) \$5,000.

3 “(C) LIMITATION ON LAND.—The term
4 ‘qualified zone business property’ shall not in-
5 clude land which is not an integral part of a
6 qualified business (as defined in section
7 1392(c)).

8 “(4) QUALIFIED ZONE PARTNERSHIP INTER-
9 EST.—The term ‘qualified zone partnership interest’
10 means any interest in a partnership if—

11 “(A) such interest is acquired by the tax-
12 payer from the partnership solely in exchange
13 for cash,

14 “(B) as of the time such interest was ac-
15 quired, such partnership was an enterprise zone
16 business (or, in the case of a new partnership,
17 such partnership was being organized for pur-
18 poses of being an enterprise zone business), and

19 “(C) during substantially all of the tax-
20 payer’s holding period for such interest, such
21 partnership qualified as an enterprise zone
22 business.

23 A rule similar to the rule of paragraph (2)(B) shall
24 apply for purposes of this paragraph.

1 “(5) TREATMENT OF SUBSEQUENT PUR-
2 CHASERS.—The term ‘qualified zone asset’ includes
3 any property which would be a qualified zone asset
4 but for paragraph (2)(A)(i), (3)(A)(ii), or (3)(A) in
5 the hands of the taxpayer if such property was a
6 qualified zone asset in the hands of any prior holder.

7 “(6) 10-YEAR SAFE HARBOR.—If any property
8 ceases to be a qualified zone asset by reason of para-
9 graph (2)(A)(iii), (3)(A)(iii), or (3)(C) after the 10-
10 year period beginning on the date the taxpayer ac-
11 quired such property, such property shall continue to
12 be treated as meeting the requirements of such
13 paragraph; except that the amount of gain to which
14 subsection (a) applies on any sale or exchange of
15 such property shall not exceed the amount which
16 would be qualified capital gain had such property
17 been sold on the date of such cessation.

18 “(7) TREATMENT OF ZONE TERMINATIONS.—
19 The termination of any designation of an area as a
20 tax enterprise zone shall be disregarded for purposes
21 of determining whether any property is a qualified
22 zone asset.

23 “(c) OTHER DEFINITIONS AND SPECIAL RULES.—
24 For purposes of this section—

1 “(1) QUALIFIED CAPITAL GAIN.—Except as
2 otherwise provided in this subsection, the term
3 ‘qualified capital gain’ means any long-term capital
4 gain.

5 “(2) CERTAIN GAIN ON REAL PROPERTY NOT
6 QUALIFIED.—The term ‘qualified capital gain’ shall
7 not include any gain which would be treated as ordi-
8 nary income under section 1250 if section 1250 ap-
9 plied to all depreciation rather than the additional
10 depreciation.

11 “(3) GAIN ATTRIBUTABLE TO PERIODS AFTER
12 TERMINATION OF ZONE DESIGNATION NOT QUALI-
13 FIED.—The term ‘qualified capital gain’ shall not in-
14 clude any gain attributable to periods after the ter-
15 mination of any designation of an area as a tax en-
16 terprise zone.

17 “(d) TREATMENT OF PASS-THRU ENTITIES.—

18 “(1) SALES AND EXCHANGES.—Gain on the
19 sale or exchange of an interest in a pass-thru entity
20 held by the taxpayer (other than an interest in an
21 entity which was an enterprise zone business during
22 substantially all of the period the taxpayer held such
23 interest) for more than 5 years shall be treated as
24 gain described in subsection (a) to the extent such
25 gain is attributable to amounts which would be

1 qualified capital gain on qualified zone assets (deter-
2 mined as if such assets had been sold on the date
3 of the sale or exchange) held by such entity for more
4 than 5 years and throughout the period the taxpayer
5 held such interest. A rule similar to the rule of para-
6 graph (2)(C) shall apply for purposes of the preced-
7 ing sentence.

8 “(2) INCOME INCLUSIONS.—

9 “(A) IN GENERAL.—Any amount included
10 in income by reason of holding an interest in a
11 pass-thru entity (other than an entity which
12 was an enterprise zone business during substan-
13 tially all of the period the taxpayer held the in-
14 terest to which such inclusion relates) shall be
15 treated as gain described in subsection (a) if
16 such amount meets the requirements of sub-
17 paragraph (B).

18 “(B) REQUIREMENTS.—An amount meets
19 the requirements of this subparagraph if—

20 “(i) such amount is attributable to
21 qualified capital gain recognized on the
22 sale or exchange by the pass-thru entity of
23 property which is a qualified zone asset in
24 the hands of such entity and which was

1 held by such entity for the period required
2 under subsection (a), and

3 “(ii) such amount is includible in the
4 gross income of the taxpayer by reason of
5 the holding of an interest in such entity
6 which was held by the taxpayer on the date
7 on which such pass-thru entity acquired
8 such asset and at all times thereafter be-
9 fore the disposition of such asset by such
10 pass-thru entity.

11 “(C) LIMITATION BASED ON INTEREST
12 ORIGINALLY HELD BY TAXPAYER.—Subpara-
13 graph (A) shall not apply to any amount to the
14 extent such amount exceeds the amount to
15 which subparagraph (A) would have applied if
16 such amount were determined by reference to
17 the interest the taxpayer held in the pass-thru
18 entity on the date the qualified zone asset was
19 acquired.

20 “(3) PASS-THRU ENTITY.—For purposes of this
21 subsection, the term ‘pass-thru entity’ means—

22 “(A) any partnership,

23 “(B) any S corporation,

24 “(C) any regulated investment company,

25 and

1 “(D) any common trust fund.

2 “(e) SALES AND EXCHANGES OF INTERESTS IN
3 PARTNERSHIPS AND S CORPORATIONS WHICH ARE
4 QUALIFIED ZONE BUSINESSES.—In the case of the sale
5 or exchange of an interest in a partnership, or of stock
6 in an S corporation, which was an enterprise zone business
7 during substantially all of the period the taxpayer held
8 such interest or stock, the amount of qualified capital gain
9 shall be determined without regard to—

10 “(1) any intangible, and any land, which is not
11 an integral part of any qualified business (as defined
12 in section 1392(b)), and

13 “(2) gain attributable to periods before the des-
14 ignation of an area as a tax enterprise zone.

15 “(f) CERTAIN TAX-FREE AND OTHER TRANSFERS.—
16 For purposes of this section—

17 “(1) IN GENERAL.—In the case of a transfer of
18 a qualified zone asset to which this subsection ap-
19 plies, the transferee shall be treated as—

20 “(A) having acquired such asset in the
21 same manner as the transferor, and

22 “(B) having held such asset during any
23 continuous period immediately preceding the
24 transfer during which it was held (or treated as
25 held under this subsection) by the transferor.

1 “(2) TRANSFERS TO WHICH SUBSECTION AP-
2 PLIES.—This subsection shall apply to any trans-
3 fer—

4 “(A) by gift,

5 “(B) at death, or

6 “(C) from a partnership to a partner
7 thereof of a qualified zone asset with respect to
8 which the requirements of subsection (d)(2) are
9 met at the time of the transfer (without regard
10 to the 5-year holding requirement).

11 “(3) CERTAIN RULES MADE APPLICABLE.—
12 Rules similar to the rules of section 1244(d)(2) shall
13 apply for purposes of this section.

14 “(g) CERTAIN BUSINESSES TREATED AS NOT
15 QUALIFIED BUSINESSES.—For purposes of this section,
16 the term ‘enterprise zone business’ has the meaning given
17 such term by section 1392 except that, in applying section
18 1392 for such purposes, the term ‘qualified business’ shall
19 not include any trade or business of producing property
20 of a character subject to the allowance for depletion under
21 section 611.

22 **“SEC. 1392. ENTERPRISE ZONE BUSINESS DEFINED.**

23 “(a) IN GENERAL.—For purposes of this subpart, the
24 term ‘enterprise zone business’ means, with respect to any

1 taxable year, any corporation or partnership if for such
2 year—

3 “(1)(A) every trade or business of such entity
4 is the active conduct of a qualified business within
5 a tax enterprise zone, and

6 “(B) at least 80 percent of the total gross in-
7 come of such entity is derived from the active con-
8 duct of such businesses,

9 “(2) substantially all of the use of the tangible
10 property of such entity (whether owned or leased) is
11 within a tax enterprise zone,

12 “(3) substantially all of the intangible property
13 of such entity is used in, and exclusively related to,
14 the active conduct of any such business,

15 “(4) substantially all of the services performed
16 for such entity by its employees are performed in a
17 tax enterprise zone,

18 “(5) at least $\frac{1}{3}$ of its employees are residents
19 of a tax enterprise zone,

20 “(6) such entity offers its employees an oppor-
21 tunity to purchase equity interests in such entity
22 and at least 5 percent (by value) of the equity inter-
23 ests in such entity are held (directly or through a
24 defined contribution plan which meets the require-
25 ments of section 401(a)) by employees who (as of

1 the time of the acquisition of the interests) were dis-
2 advantaged residents of a tax enterprise zone,

3 “(7) less than 5 percent of the average of the
4 aggregate unadjusted bases of the property of such
5 entity is attributable to collectibles (as defined in
6 section 408(m)(2)) other than collectibles that are
7 held primarily for sale to customers in the ordinary
8 course of such business, and

9 “(8) less than 5 percent of the average of the
10 aggregate unadjusted bases of the property of such
11 entity is attributable to nonqualified financial prop-
12 erty.

13 “(b) DISADVANTAGED RESIDENTS.—For purposes of
14 subsection (a), an employee is a disadvantaged resident
15 of a tax enterprise zone if such employee is a resident of
16 such zone and if—

17 “(1) such employee is a member of an economi-
18 cally disadvantaged family (within the meaning of
19 section 51(d)(11)), or

20 “(2) the family income (within the meaning of
21 section 143(f)(2)) of such employee is less than 50
22 percent of the applicable median family income (as
23 defined in section 143(f)(4)).

24 “(c) QUALIFIED BUSINESS.—For purposes of this
25 section—

1 “(1) IN GENERAL.—Except as otherwise pro-
2 vided in this subsection, the term ‘qualified business’
3 means any trade or business.

4 “(2) RENTAL OF REAL PROPERTY.—The rental
5 to others of real property located in a tax enterprise
6 zone shall be treated as a qualified business if and
7 only if—

8 “(A) in the case of real property which is
9 not residential rental property (as defined in
10 section 168(e)(2)), the lessee is an enterprise
11 zone business, or

12 “(B) in the case of residential rental prop-
13 erty (as so defined)—

14 “(i) such property was originally
15 placed in service after the date the tax en-
16 terprise zone was designated, or

17 “(ii) such property is rehabilitated
18 after such date in a rehabilitation which
19 meets requirements based on the principles
20 of section 42(e)(3).

21 “(3) RENTAL OF TANGIBLE PERSONAL PROP-
22 ERTY.—The rental to others of tangible personal
23 property shall be treated as a qualified business if
24 and only if substantially all of the rental of such

1 property is by enterprise zone businesses or by resi-
2 dents of a tax enterprise zone.

3 “(4) TREATMENT OF BUSINESS HOLDING IN-
4 TANGIBLES.—The term ‘qualified business’ shall not
5 include any trade or business consisting predomi-
6 nantly of the development or holding of intangibles
7 for sale or license.

8 “(5) CERTAIN BUSINESSES EXCLUDED.—The
9 term ‘qualified business’ shall not include—

10 “(A) any trade or business consisting of
11 the operation of any facility described in section
12 144(c)(6)(B), and

13 “(B) any trade or business the principal
14 activity of which is farming (within the meaning
15 of subparagraphs (A) or (B) of section
16 2032A(e)(5)), but only if, as of the close of the
17 preceding taxable year, the sum of—

18 “(i) the aggregate unadjusted bases
19 (or, if greater, the fair market value) of
20 the assets owned by the taxpayer which are
21 used in such a trade or business, and

22 “(ii) the aggregate value of assets
23 leased by the taxpayer which are used in
24 such a trade or business,

25 exceeds \$500,000.

1 For purposes of subparagraph (B), rules similar to
2 the rules of section 1395(b) shall apply.

3 “(d) NONQUALIFIED FINANCIAL PROPERTY.—For
4 purposes of this section, the term ‘nonqualified financial
5 property’ means debt, stock, partnership interests, op-
6 tions, futures contracts, forward contracts, warrants, no-
7 tional principal contracts, annuities, and other similar
8 property specified in regulations; except that such term
9 shall not include—

10 “(1) reasonable amounts of working capital
11 held in cash, cash equivalents, or debt instruments
12 with a term of 18 months or less, or

13 “(2) debt instruments described in section
14 1221(4).

15 **“SEC. 1393. TAX ENTERPRISE ZONE.**

16 “For purposes of this subchapter, the term ‘tax en-
17 terprise zone’ means any area hereafter designated as an
18 enterprise zone or tax enterprise zone pursuant to any law
19 enacted after the date of the enactment of this section.”

20 (b) CLERICAL AMENDMENT.—The table of sub-
21 chapters for chapter 1 of such Code is amended by insert-
22 ing after the item relating to subchapter T the following
23 new subchapter:

“SUBCHAPTER U—Capital gain exclusion for investments in en-
terprise zones.”



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